

**ORIGINAL
FILED**

MAR 2 2 2004

CLERK, U.S. DISTRICT COURT
EASTERN DISTRICT OF CALIFORNIA

BY

DEPUTY CLERK

1 TIMOTHY J. HATCH, SBN 165369
2 BRYAN B. ARNOLD, SBN 151583
3 DARREN LISITZA, SBN 225824
4 GIBSON, DUNN & CRUTCHER LLP
5 333 South Grand Avenue
6 Los Angeles, California 90071-3197
7 Telephone: (213) 229-7000
8 Facsimile: (213) 229-7520

6 CHARLES J. STEVENS
7 BRAD BENBROOK
8 STEVENS & O'CONNELL LLP
9 400 Capital Mall, Suite 1400
10 Sacramento, CA 95814-4412
11 Telephone: (916) 329-9111
12 Facsimile: (916) 329-9110

10 Attorneys for Defendant,
11 UNIVERSITY OF PHOENIX

12 UNITED STATES DISTRICT COURT
13 EASTERN DISTRICT OF CALIFORNIA

15 UNITED STATES OF AMERICA, *ex rel.*
16 MARY HENDOW and JULIE ALBERTSON,

17 Plaintiffs,

18 v.

19 UNIVERSITY OF PHOENIX and DOES 1-500,
20 Inclusive,

21 Defendants.

CASE NO. CIV. S-03-0457 GEB DAD

**DEFENDANT'S MEMORANDUM OF
POINTS AND AUTHORITIES IN SUPPORT
OF ITS MOTION TO DISMISS RELATORS'
SECOND AMENDED COMPLAINT
PURSUANT TO FEDERAL RULE OF CIVIL
PROCEDURE 12(b)(6)**

Date: May 3, 2004

Time: 9:00 a.m.

Place: Courtroom 10

Judge: Hon. Garland E. Burrell, Jr.

TABLE OF CONTENTS

1
2
3
4
5
6
7
8
9
10
11
12
13
14
15
16
17
18
19
20
21
22
23
24
25
26
27
28

	<u>Page</u>
I. INTRODUCTION.....	1
II. FACTUAL AND PROCEDURAL BACKGROUND.....	2
A. The University of Phoenix	2
B. Relators' Allegations	3
1. Alleged Violation of HEA Requirements	3
2. Alleged False Claims	3
3. Alleged False Certifications of Compliance with HEA Compensation Rules.....	4
C. Procedural Posture	4
III. RELATORS HAVE FAILED TO STATE A CLAIM UNDER THE FCA AND THEIR COMPLAINT MUST BE DISMISSED WITH PREJUDICE	5
A. Relators' Claims Fail Because They Still Have Not Alleged Sufficient Facts to Establish that UOP Submitted or Caused to Be Submitted a False Claim.....	5
B. Relators' Claims Fail Because They Have Not Identified a Certification of Compliance with Federal Limits on Incentive Compensation on Which Government Payment Was Conditioned.....	10
1. PPAs, Which Set Forth the Conditions Under Which Schools May Participate in Financial Aid Programs, Are Not Certifications of Compliance with Those Requirements Nor Is Government Payment of Financial Aid Conditioned on Any Alleged Certification in the PPA	10
2. Management Assertion Letters UOP Submitted to Its Independent Auditors Are Not Actionable Certifications Under the FCA.....	15
3. UOP Certifications of Student Eligibility for FFELP Loans on Applications Students Submit to Third Party Lenders Are Not Certifications of UOP's Compliance with Title IV HEA Requirements.....	17
IV. CONCLUSION	18

TABLE OF AUTHORITIES

1
2
3
4
5
6
7
8
9
10
11
12
13
14
15
16
17
18
19
20
21
22
23
24
25
26
27
28

Page(s)

Cases

Chambers v. Time Warner, Inc., 282 F.3d 147 (2nd Cir. 2002) 5

Cruz v. Beto, 405 U.S. 319 (1972) 5

Harrison v. Westinghouse Savannah River Co., 176 F.3d 776 (4th Cir. 1999) 6, 7, 16

Morely v. Walker, 175 F.3d 756, 759 (9th Cir. 1999) 5

Pareto v. FDIC, 139 F.3d 696 (9th Cir. 1998) 5

United States ex rel. Clausen v. Laboratory Corp. of Am., Inc., 290 F.3d 1301 (11th Cir. 2002) *cert. denied*, 537 U.S. 1105 (2003) 6

United States ex rel. Coppock v. Northrop Grumman Corp., Civil Action No. 3:98-CV-2143-D, 2002 U.S. Dist. Lexis 14510, at *43 (N.D. Tex. August 1, 2002) 15

United States ex rel. Gay v. Lincoln Technical Institute, Inc., Civ. Act. No. 3:01-CV-505-K (N.D. Tex. 2003) 1, 2, 17

United States ex rel. Graves v. ITT Educational Services, Inc., 284 F. Supp. 2d 487 (S.D. Tex. 2003) passim

United States ex rel. Hopper v. Anton, 91 F.3d 1261 (9th Cir. 1996), *cert. denied*, 519 U.S. 1115 (1997) passim

United States ex rel. Lee v. Smithkline Beecham Clinical Labs., Inc., 245 F.3d 1048, 1053 n.4 (9th Cir. 2001). 10

United States ex rel. Marcus v. Hess, 317 U.S. 537 (1943) 5

United States, ex rel. Plumbers & Steamfitters Local Union v. C.W. Roen Constr. Co., 183 F.3d 1088, 1092 (9th Cir. 1999) 17

United States ex rel. Rakow v. Pro Builders Corp., 2000 U.S. Dist. LEXIS 21832 at *13 (D. Mont. 2000) 13

United States ex rel. Thompson v. Columbia/HCA Healthcare Corp., 125 F.3d 899 (5th Cir. 1997) 10, 16

United States ex rel. Willard v. Humana Health Plan of Texas Inc., 336 F.3d 375 (5th Cir. 2003) 6

United States v. Kitsap Physicians Service, 314 F.3d 995 (9th Cir. 2002) 6

United States v. Rivera, 55 F.3d 703 (1st Cir. 1995) 6, 9

United States v. Vanoosterhout, 898 F. Supp. 25 (1995) 9

Statutes

Cal. Ed. Code § 56205(a) 13

20 U.S.C. § 1413(b) 13, 14

31 U.S.C. § 3729(c) 6

31 U.S.C. § 3729(a)(1) 6, 10

31 U.S.C. § 3729(a)(2) 6

31 U.S.C. § 3730 1

31 U.S.C. § 3730(b)(2) 4

1
2
3
4
5
6
7
8
9
10
11
12
13
14
15
16
17
18
19
20
21
22
23
24
25
26
27
28

Rules

34 C.F.R. § 300.141 14
34 C.F.R. § 300.600 13
34 C.F.R. Part 600..... 15
34 C.F.R. Part 668..... 15
34 C.F.R. § 668.14(b) 14
34 C.F.R. § 668.23(a)(2) 15, 16
34 C.F.R. § 668.23(a)(4) 16
34 C.F.R. § 668.23(b)(3)(ii) 16
34 C.F.R. § 668.162(a)..... 7
34 C.F.R. § 668.162(b)..... 7
34 C.F.R. § 668.164(a)..... 7
34 C.F.R. § 668.165(b)..... 8
34 C.F.R. § 668.166(a)..... 8
34 C.F.R. § 668.167(b)..... 8
34 C.F.R. § 682.100(a)..... 7
34 C.F.R. § 682.603(a)..... 18
34 C.F.R. § 682.604(a)..... 8
34 C.F.R. § 690.1 7

Other Authorities

5 Wright & Miller, *Federal Practice and Procedure* § 1363 5

1 **I. INTRODUCTION**

2 This is the third attempt by relators Mary Hendow and Julie Albertson to state a claim against
3 the against the University of Phoenix ("UOP") pursuant to the False Claims Act, 31 U.S.C. § 3730
4 (the "FCA"). Styled as a "false certification" case, relators contend UOP violated recruiter
5 compensation restrictions contained in the Higher Education Act ("HEA") and the implementing
6 regulations of the Department of Education ("ED") by paying its recruiters a salary based on
7 enrollment activities. Second Amended Complaint ("SAC") ¶ 1. Relators contend UOP falsely
8 certified compliance with the HEA restrictions through execution of Program Participation
9 Agreements ("PPAs") in which UOP stated it would comply with the HEA, SAC ¶ 24, and by
10 submitting "management assertion letters" to its independent auditors in which it purportedly certified
11 its compliance with HEA limits on incentive compensation.

12 Through this action, relators are attempting to turn what amounts to no more than allegations
13 of regulatory violations into a FCA case. As explained by the Ninth Circuit, the FCA is not a vehicle
14 to enforce regulatory compliance. *United States ex rel. Hopper v. Anton*, 91 F.3d 1261, 1267 (9th
15 Cir. 1996), *cert. denied*, 519 U.S. 1115 (1997) ("Mere regulatory violations do not give rise to a
16 viable FCA action."). In fact, three District Courts have recently dismissed FCA complaints against
17 educational institutions based on virtually identical theories as those raised by relators.¹ The relators'
18 claims suffer from the same basic defects.

19 First, the relators have not identified any claim purportedly submitted by UOP to which FCA
20 liability could attach. Relators alleged that UOP submitted false claims by requesting money from
21 ED and third party lenders to disburse financial aid to students. SAC ¶¶ 33, 35. Under the regulatory
22

23 ¹ These matters are *United States ex rel. Graves v. ITT Educational Services, Inc.*, 284 F. Supp. 2d
24 487 (S.D. Tex. 2003) (hereinafter *Graves*); *United States ex rel. Gay v. Lincoln Technical*
25 *Institute, Inc.*, Civ. Act. No. 3:01-CV-505-K (N.D. Tex. 2003) (hereinafter *Gay*); and *United*
26 *States ex rel. Bowman v. Education America, Inc.*, Civ. Act. No. H-00-3028, p. 3-4 (S.D. Tex.
27 January 8, 2004) (hereinafter *Bowman*). In the *Bowman* matter, the court rejected similar claims
28 filed against another educational institution, stating that "[b]ecause this case presents virtually
 identical claims arising under the same theory of liability that previously has been repeatedly
 rejected, the Court expressly adopts and follows the rationale of Judge Rosenthal's well-reasoned
 and thorough opinion" in the *Graves* matter. The *Gay* and *Bowman* decisions are attached as
 Exhibits A and B to the Request for Judicial Notice, filed concurrently. The *Graves* and *Gay*
 decisions have been appealed to the Fifth Circuit.

1 scheme, however, UOP is responsible for administering the financial aid program, which includes
2 disbursing funds to eligible students. 34 C.F.R. § 668.162. UOP does not submit a claim or demand
3 for payment, but only for the amount it needs to fulfill the government's (and third party lender's)
4 commitments to financial aid recipients. The fact UOP may be in possession of government funds is
5 not sufficient to trigger liability under the FCA. *Hopper*, 91 F.3d at 1265.

6 Second, relators have not alleged facts sufficient to establish that any purported claim was
7 false or fraudulent. In a false certification case, a relator must establish that the defendant has: (1)
8 made an affirmative certification of compliance with a statute or regulatory requirement; and (2) the
9 certification is a condition of payment. *Id.* at 1266 (false certification creates FCA liability "when
10 certification is a prerequisite to obtaining a government benefit"). Relators can meet neither prong.

11 Relators assert that PPAs executed by UOP and management assertion letters UOP provides
12 to its independent auditors constitute false certifications, but have not shown how either of these
13 documents can be construed as "certifications of compliance" with the HEA incentive compensation
14 limits. The bottom line is that there is nothing in statute or regulation that requires UOP to certify its
15 compliance with these limitations. The *Graves* and *Gay* courts rejected claims by relators that the
16 PPAs and management assertion letters constituted certifications of compliance actionable under the
17 FCA. Relators have not alleged any facts that distinguish their case from those decisions.

18 **II. FACTUAL AND PROCEDURAL BACKGROUND**

19 **A. The University of Phoenix**

20 Founded in 1976, the UOP is the largest private university in the United States. UOP's
21 primary mission is to educate working adults to develop the knowledge and skills that will enable
22 them to achieve their professional goals, improve the productivity of their organizations, and provide
23 leadership and service to their communities. UOP's adult learning model makes higher education
24 more accessible, efficient, and relevant to the real world, as adult learners bring to the classroom
25 organizational and personal experiences that enrich the learning process.

26 Accredited by the Higher Learning Commission of the North Central Association in 1978,
27 UOP offers both undergraduate and graduate programs in a variety of fields. UOP currently enrolls
28

1 201,381 degree seeking adult students at 51 campuses (including its on-line campuses) and 91
2 learning centers in 29 states.

3 **B. Relators' Allegations**

4 **1. Alleged Violation of HEA Requirements**

5 Relators Mary Hendow and Julie Albertson are Enrollment Counselors at UOP's Northern
6 California campus. SAC. ¶¶ 5-6. The Complaint alleges that UOP is the largest recipient of federal
7 student financial aid funds from ED pursuant to the HEA, Title IV. SAC. ¶ 1. Relators suggest the
8 HEA prohibits "universities from providing 'any commission, bonus or other incentive payment . . .'
9 to recruiters based on recruiting activities." SAC ¶ 14.

10 Relators allege that UOP violates the restrictions on "commission, bonus, or other incentive
11 payments" by paying its Enrollment Counselors a salary based upon the number of students they
12 enroll and other enrollment activities, such as telephone calls, generation of leads, and appointments.
13 SAC ¶ 39. Relators contend that Enrollment Counselors also receive trips, gifts, and contest awards
14 based upon the number of enrollments and enrollment activities. SAC ¶ 49.

15 **2. Alleged False Claims**

16 Relators allege that UOP submitted two types of false claims. First, relators contend that UOP
17 submitted false claims within the meaning of the FCA by submitting a request for Pell Grant funds to
18 ED. SAC ¶ 33. Relators do not contend that student applications for Pell Grants constitute false
19 claims. Rather, relators suggest that UOP's request for funds to ED necessary to administer the Pell
20 Grant program and disburse Pell Grant funds to students constitutes a false claim. *Id.* Relators
21 contend that UOP credits the Pell Grant funds UOP receives from ED to UOP students for tuition. *Id.*

22 Relators also contend that UOP submitted false claims in connection with government-insured
23 loans under the Federal Family Education Loan Program ("FFELP"). SAC ¶ 35. Relators contend
24 that "UOP submits the request for those funds directly to a private lender," who transfers funds
25 directly into a UOP account. *Id.* These loans made by private lenders are guaranteed by state
26 agencies and non-profit organizations, which reimburse the lender if a student defaults. SAC ¶ 37. If
27 a guaranty agency cannot collect from the student, ED reimburses the agency. SAC ¶ 37. Relators
28 contend that the government pays interest on these loans while students are enrolled in classes and

